

IN THE
United States
Circuit Court of Appeals,
FOR THE NINTH CIRCUIT.

John P. Carter, Former Collector of
Internal Revenue for the Sixth Dis-
trict of California,

Plaintiff in Error.

vs.

Jacob Bauman,

Defendant in Error.

OPENING BRIEF OF PLAINTIFF IN ERROR.

SAMUEL W. McNABB,
United States Attorney,

DONALD ARMSTRONG,
Assistant United States Attorney,
Attorneys for Plaintiff in Error.

No. 5098.

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This is an appeal from the judgment of the United States District Court for the Southern District of California in which the lower court allowed the recovery of the sum of \$1805.98, the amount of taxes assessed and collected by the plaintiff in error from the defendant in error upon 820.9 gallons of grape brandy which was stolen from the fortifying room of the bonded winery of defendant in error.

The facts are undisputed and are as follows:

That on the 15th day of November, 1920, and for sometime prior thereto, the defendant in error was the

owner and proprietor of Bonded Winery No. 5, within the Sixth Internal Revenue Collection District of California; that there was situated on these bonded premises a fortifying room in which the brandy in question was stored; that sometime during the evening of November 15th, 1920, the brandy was stolen from said fortifying room.

The only question presented to the court below and urged in this appeal is whether the fortifying room situated on premises constituting a bonded winery is a "distillery or other bonded warehouse" within the meaning of section 5 of an act supplemental to the National Prohibition Act, known as the Willis-Campbell Act (42 Stat. 222, Comp. St. Ann. Supp. 1923, Secs. 10138 4/5 (d) and 10138 4/5 (e)), which reads in part as follows:

"Distilled spirits upon which the internal revenue tax has not been paid are * * * lost by theft from a distillery or other bonded warehouse, and it shall be made to appear to the Commissioner that such losses did not occur as the result¹ of negligence, connivance, collusion or fraud on the part of the owner or person legally accountable for such distilled spirits, no tax shall be assessed or collected upon the distilled spirits so lost, nor shall any tax penalty be imposed or collected by reason of such loss, but the exemption from the tax and penalty shall only be allowed to the extent that the claimant is not indemnified against or recompensed for such loss. This provision shall apply to any claim for taxes or penalties that may have occurred since the passage of the National Prohibition Act or that may occur hereafter. Nothing in this section shall be construed as in any manner limiting or restricting the provision of Title III of the National Prohibition Act."

It is the position of plaintiff in error that Congress did not intend to exempt the fortifying room of a bonded winery from payment of taxes upon the loss or theft of grape brandy therefrom by section 5 of the Willis-Campbell Act, *supra*, and that the words "distillery or other bonded warehouse" do not include the fortifying room of a bonded winery either within the meaning of said section or in ordinary or common parlance, and in support thereof respectfully submits the following:

Distillery warehouses are established under the provisions of section 3271, R. S., as amended, which section provides among other things that the warehouse shall be under the direction and control of the Collector of Internal Revenue of the Collection District in which it is situated and in charge of an Internal Revenue storekeeper assigned thereto by the Commissioner. Such bonded warehouse was held to be an agency of the Government in the case of *George v. Fourth National Bank of Lanesville* (41 Fed. 263). By virtue of 3251, R. S., as amended, the Government has an express lien on spirits in such warehouse,—on the buildings and land constituting the distillery premises.

That distillery warehouses are under the direction and control of the Collector of the District and in charge of an Internal Revenue storekeeper gauger assigned thereto by the Commissioner, see sections 3153, 3154, 3274, 3260 and 3293, R. S., as amended. In this connection attention is directed to the provisions pertaining to the establishment of distillery warehouses. A distiller must provide the warehouse at his own expense, which must be built in accordance with the provisions of section 3271, R. S., and Treasury Decision 2431. When thus constructed,

application must be made to the Commissioner of Internal Revenue for its establishment, and the application is required to be accompanied by a diagram of the warehouse and a certificate of examination by the Collector. The warehouse is then formally approved in writing by the Commissioner of Internal Revenue, the notice of approval containing a complete description of the warehouse, and storekeepers or storekeeper-gaugers must be assigned thereto by the Commissioner, formal notice being sent to the storekeeper or storekeeper-gauger and Collector, a record thereof being made in the office of the Commissioner.

Sections 51 and 52 of the Act of August 27, 1894 (28 Stat. 509) and pages 247 and 248 of the Compilation of Internal Revenue Laws of 1920 provide for the establishment of general bonded warehouses and contain much the same provision for the assignment of officers, placing the control of the warehouses in the Collector of Internal Revenue of the District and the joint custody of the storekeeper and the proprietor thereof.

The Act of March 3, 1877, as amended (19 Stat. 335, pages 251 and 252 of the Compilation of Internal Revenue Laws of 1920), provides for the establishment of special bonded warehouses for the storage of fruit, brandy. Section 1 thereof provides that each such warehouse shall be in charge of a storekeeper to be appointed, assigned, transferred, etc., in the same manner as storekeeper-gaugers at distillery warehouses, and further provides that every such warehouse shall be under the control of the Collector of Internal Revenue for the district in which located and shall be in the joint custody of the storekeeper and proprietor thereof.

The foregoing bonded warehouses are evidently the ones contemplated in section 5, Act of November 23, 1921, by the phrase "distillery or other bonded warehouse". It is only fair to assume that the Government by reason of the precautions in the establishment of and supervision over the foregoing warehouses intended to exempt the taxpayer from taxes on liquors lost at such warehouses.

The foregoing provisions of law and regulations pertaining to distillery and bonded warehouses do not, however, apply to the fortifying rooms of bonded wineries. Bonded wineries, including the fortifying rooms, are established and supervised in accordance with the provisions of sections 612 and 617 of the Revenue Act of 1918, approved February 24, 1919, section 612 reading in part as follows:

"That under such regulations and official supervision and upon the giving of such notices, entries, bonds, and other security as the Commissioner, with the approval of the Secretary, may prescribe, any producer of wines defined under the provisions of this title, may withdraw from any fruit distillery or special bonded warehouse grape brandy, or wine spirits, for the fortification of such wines on the premises where actually made * * *."

Section 617, amending sections 42, 43 and 45 of the Act of October 1, 1890, as amended, reads in part as follows:

"That any producer of pure sweet wines may use in the preparation of sweet wines, under such regulations and after the filing of such notices and bonds, together with the keeping of such records and the rendition of such reports as to materials and prod-

ucts as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe, wine spirits produced by any duly authorized distiller * * *.”

Section 4, subdivision (b) of regulation 28, part I of the Commissioner of Internal Revenue, drawn and adopted pursuant to sections 612 and 617 of the Revenue Act of 1918 and approved by the Secretary of the Treasury, reads as follows:

“A winery, where wine is to be fortified, in all cases will consist of a room to be known as the fortifying room.”

Section 17 of said regulations reads in part as follows:

“When a winemaker desires to begin the fortification of sweet wines, he will make a request for the assignment of an officer to supervise the fortification of such wine.”

The fortifying room, although part of the bonded premises and thus “bonded” is not a warehouse as that term is used either in the revenue laws or regulations or in common parlance. A fortifying room is used principally as an incident to the manufacture of wine and not for the storage of distilled spirits as the brandy or distilled spirits are withdrawn from a distillery or bonded warehouse as is evidenced by sections 612 and 617 of the Revenue Act of 1918. Spirits may be kept on hand or stored in this room but such a use occurs after the spirits have been taken out of the warehouse where the loss occurring would be allowable and is held pending its use in the manufacture of sweet wines. It is thus substantially a manufacturing use and does not convert a manufacturing plant into a warehouse. A distillery or other

bonded warehouse is strictly one defined by statute as has been heretofore shown, while the fortifying room of a bonded winery is created and supervised by regulation of the Commissioner of Internal Revenue.

It is, therefore, respectfully urged that Congress did not intend to include the fortifying room of a bonded winery within the meaning of section 5 of the Willis-Campbell Act, *supra*, and that the judgment of the lower court should be reversed and judgment entered for the plaintiff in error.

Respectfully submitted,

SAMUEL W. MCNABB,

United States Attorney,

DONALD ARMSTRONG,

Assistant United States Attorney,

Attorneys for Plaintiff in Error.

